# THE BUTTER MARKET

Before the fall of prices of food-stuffs in November-December, 1910, there had been much talk as to the causes of high prices. Various remedies were suggested. Reformers prophesy that unless serious measures are taken by the government, prices will continue to go up endlessly. Complaints, however, were all silenced at the end of last year. Prices of butter, eggs, and many other food-stuffs began to drop and finally reached, in January, 1911, a level lower than which they have not fallen in the memory of produce dealers. While a study of the butter market cannot be expected to settle the problem of high cost of living, yet it clearly shows that the situation is not hopeless and that high prices for the necessaries of life are subject to economic laws, safely setting limits above and also below which prices can go but temporarily.

Officially the price of butter is fixed at the "Produce Exchanges" in Chicago and New York. It is fixed as prices are established on bonds and stocks on the floors of stock exchanges. So much is offered by the present buyers, so much is wanted by the seller—the difference, is of course, always very small—and if a transaction is made the price is settled for this particular day. It is evident, that, with the exception of particularly lively speculative activities, the part this official bidding plays in fixing prices is only formal; it is the expression and the end of a process that had already taken place. Changes in supply and demand, opinions as to the state of the market in general, are determined independently of and prior to the work on the floor of the Produce Exchange. The bidding there determines only the tendency of the market, and the price of butter would, if I may anticipate, hardly change to any extent should the Produce Exchange cease to quote butter.

What then are the underlying forces working in the butter-price-making process? Some general remarks on the nature of the butter market will serve to facilitate the understanding of the discussion. Usually butter is at its lowest in May. Storage butter

is then already used up; fresh butter is coming in in small quantities; dealers do not buy yet for the coming season. They order for the present use only; the market is at a standstill. Activity begins in June, continuing down to the middle of September. The market steadily advances during these months in normal years, sharp rises depending only on serious damages to the hay crop. The price paid by the dealers in the summer months is usually referred to as the storage price, for in these months most of the big dealers store away butter to be used till next spring. Very little fresh butter is made in the winter months, and although the exchange quotations mentions the price of fresh butter, all transactions are understood to refer to cold-storage butter.

During the years 1900–9 butter was steadily advancing, every successive storing season showing a higher price than the former year. Naturally the prices in the winter months showed corresponding advances. While this apparently normal development of the butter business was taking place, people in the business began to wonder as to the causes of yearly advances in the price. It is natural that butter should be higher in winter than in summer, but that every successive summer should see a rise above the preceding summer was considered abnormal by dealers in spite of the steadiness of the movement upward. They knew too well that this movement could not keep up for a long period. In fact, many dealers in the East were so sure of an approaching fall in prices that in 1909–10 they speculated on it by refusing to store butter. This means that they had decided to buy only in small quantities, expecting to be able to buy, in winter, the same storage butter at a lower price than they would have to pay for it in the regular summer storing months. They miscalculated, however, and in spite of the obviousness of their reasons in refusing to store butter in 1909—reasons which were as true, if not more so, for the 1910 season—they all returned to the usual methods. Dealers accordingly paid 36, 37, and 38 cents for butter in the summer of 1910; adding storage expenses and interest, the price was expected to be at least 46 cents.

It is of course difficult to answer the question why the crash took place in 1910 and not in 1909, or why the "bullish" movement did

not keep up to 1911. Two facts are certain: first, the movement had to continue long enough to bring about the effect of the undermining forces, and second, this movement could not keep up indefinitely, for with its growth it also developed these negative forces, destined to break the market. To be sure, there is a minimum below which the price of butter cannot fall. Aside from the fact that the price must be high enough to induce the farmer to keep the cows, pay rent for the grass-land, and pay for his labor, the price must also be sufficient to keep the farmer from selling his products in the form of milk, cheese, and cream, etc. While it is true that the Nebraska farmer cannot very well sell all his milk, owing to remoteness of large cities, he can always find a sufficient market for his cream if he cannot get for the butter a remunerative price. There are, then, two forces setting a minimum limit of the price of butter: cost of production and the price of related products. Twenty-five cents a pound is considered by experts to be this minimum. True enough, in January, 1911, good butter was offered at 18 cents to the retail trade, but this referred only to butter on hand and was due only to the crisis in the butter market. As to the maximum which butter can reach in normal years (scarce years not included), no definite figure can be set, yet that there is a maximum is sufficiently shown by the experience of the last few years.

No one in the butter business can tell exactly which of the many factors making and unmaking the price of butter was the most active in the crisis last year. It is, however, popularly admitted that speculation was one of the chief causes, particularly so because it is comparatively new in the butter trade. The only form of speculation known to butter dealers prior to 1906–7 was of the simplest kind, and it referred only to the storage of butter in the summer months so as to keep the price high in the summer when butter would otherwise be low on account of the large supply, as well as to obtain a higher price for it in the winter months.

A serious agitation is carried on in the eastern states against cold storages just on account of their supposed influence upon prices. We are not concerned here with the hygiene or sanitary side of the question. Everybody will admit that but for cold-storage, butter,

like many other food-stuffs, would be very cheap during the summer months; but people ignore the fact that butter would be prohibitively high in winter. So from a social standpoint the sum total paid out for butter would be the same; so many units at, say, 25 cents and so many, say, at $1.00 a pound would bring in for butter as much as at present when the total supply is sold at about 32 cents a pound. There may be some validity in the argument according to which poor people should be given the chance to eat butter when it is low and refrain from eating butter when it is naturally high, as is being done with fruit and certain green-stuffs. But taking into consideration first, that the summer supply cannot possibly be consumed in the summer months at a paying price; second, that the summer output is so much larger than that of the rest of the year that the average increase of price is not in any sense prohibitive, taking 25 cents as the minimum; and, lastly, that providing of food-stuffs for the future is so natural, we can safely accept the existence of cold storages and their influence upon price not only as a necessary evil but as wholesome economic phenomena. The problem here, as in so many other instances, is how to retain the good while keeping out the evil results.

And it is just because the cold-storage houses have performed more than their normal functions in the years preceding the crisis that they made popular agitation not only possible but justifiable. They not only kept butter from spoiling but speculated in it in these years, thus introducing elements foreign and ruinous to the butter business. Their only justification is that they were driven to it, driven in the commercial sense of the word, so to say, by the march of events. Here is how it happened. In the years 1902–5 the profits of the butter dealers attracted the attention of outside capitalists; not that they cared to enter the butter business proper, but that they wanted to reap a part of the profits by coming in between the creamery and the dealers. They bought butter to resell it to the latter. The immediate result was one which is customary in bullish markets. Prices went up. Moreover the problem of ascertaining the actual demand became more complex. A false, unreal, speculative demand was created on the top of the market and people became freer in their purchases, steadily boosting

up the price, unmindful temporarily of the work of the slowly operating negative forces such as limited demand, decreasing consumption, substitutes and imports, the influence of which is taken up below. Dealers themselves naturally were affected—they too began to speculate. To their assistance came the storage houses, which were, of course, anxious to increase the amount of goods put away in storage. The cold-storage business became so profitable that it invited serious competition and new methods to attract the dealer became necessary. Lowering the rates for storing was not enough of an inducement and it would cut the profits. To begin with, they took over the very legitimate work of lending money on butter at the regular banking rates. Dealers cannot usually afford to lay out all the capital necessary to finance the storing of butter and they will rather borrow the money from cold storages than from banks, if not for any other reason than to be able to take out butter the moment they need it without going for the bank's release. Then there is the advantage of having a larger balance in the bank for an extra day.

But storage houses soon began to compete as to the amount lent on each tub of butter. For instance, up to 1908 the Quincy Cold Storage house had monopoly over the storage business in Boston. They did the legitimate business of keeping the butter in a certain temperature, leaving lending operations to the banks. The Boston Terminal Storage, when opening up in Boston in 1909, started at once to lend money on butter. The Quincy House had to follow. From $10 per tub the amount lent soon went up to $13, and finally the Boston Terminal, backed by capitalists, began to give $16 on each 60 lbs. tub of butter. Moreover they would allow a dealer to buy butter on drafts, attending themselves to the payment of the latter and collecting from the dealers the difference between $16 and the actual cost of the tub of butter. Thus the dealer had to invest very little—three or four dollars per tub. The result was that buying became very easy and dealers instead of storing the normal quantity that they were accustomed to sell to their trade began to speculate, buying for the sake of reselling to other dealers, who might go short.

The question arises here what became of the butter. Obviously,

one may think, it was consumed at higher prices, even if the consumption was accompanied by complaints at the high cost of living. Here again the existence of cold-storage houses served to cover the corresponding change in demand. The truth of the matter is that all of the butter was not consumed. To be sure many consumers, unable to go without butter, kept on paying higher prices; but people to whom 10 or 15 cents on a pound of butter means a great deal used less of it, at the same time accustoming their digestion to butterine and oleomargarine. What then happened to the surplus supply of butter? The answer to this at once suggests the border line between the good and evil involved in the cold storage. The natural and the customary period for keeping butter in cold storage extends from July to the end of March. The output between March and the end of June is usually equal to the demand at customary prices. People then should have fresh butter during this period, and correspondingly cold storages should remain empty up to the end of June. Beginning with 1904 these storing periods began to move forward at the end and backward at the beginning of the period. In 1909 there was plenty of storage butter at the end of April and new storing began exceptionally early in June. Owing to high prices consumers had to use storage butter in April; speculation kept the price for the fresh butter high enough with a view to the new storing season, so a smooth surface was kept on the butter market. It is obvious that a crash had to come, since carrying over butter from one season to another, even if possible from the point of view of preserving the butter in good shape, is a very risky enterprise, practicable only when the approach of a famine is certain. But such a conjuncture never actually takes place. Moreover early butter, coming in in May and June, cannot stand storage. Thus the supply in one year was consumed at the expense of storing the supply of the coming year and so on until if it had not been for the crisis we should soon have reached the impossible situation of keeping a constantly increasing supply with correspondingly decreasing demands. As said before, many dealers expected the crisis early in 1910 and lost heavily by being forced to pay high prices to speculators, who continued to be optimistic.

Other forces, too, were active in undermining the upward price movement. They are worth consideration both in their connection with the butter market and on account of their significance in the price-making process in general. First come the substitutes. When the crash came and dealers were forced by banks and a general oversupply to offer their butter at any price in January and February, 1911, the writer had the interesting experience of trying, and unsuccessfully at that, to sell butter to the retail stores in Nashua, N.H., below the price of butterine. "We cannot afford," was the reply, "to get our customers back to butter for a short period till the panic is over and then begin a new campaign in putting butterine on the market." There is a creamery store in Chicago where one cannot buy a pound of actual butter, even if one is willing to pay the price. Butter was simply driven out from many markets. Some consumers are aware of it; most do not care to know the truth. Of course, the price of the substitute is also likely to go up with the increased demand and is in turn controlled by the prices of the superior article. In the early months of last year butterine was in turn driven out in some places by the fall of butter prices.

Next in importance comes the question of importing butter from abroad. Canada is, of course, the only possible source. Maine, Vermont, Massachusetts, New Hampshire, actually attempted importing butter from Canada, paying five cents duty per pound. But dealers discovered a more convenient way of fighting high prices and cheating the government at the same time. They imported cream and churned butter on this side of the fence, the duty on cream being only 50 cents per jug, 80 lbs.—40 per cent cream—which amounts to 50 cents duty on 35 lbs. of butter. All creameries on Prince Edward Island, for instance, closed their cheese factories in 1909–10 and shipped their cream to Boston. Eastern dealers, afraid of the growing independence of the western farmer (for the latter surely benefited by the high prices of food-stuffs), seriously began to think of establishing creameries in the East, relying upon Canada for raw materials, and they eagerly looked forward to reciprocity tariffs with that country. Potential imports thus threaten bullish movements on food-stuffs at home.

To conclude, the maximum price for butter is firmly determined on one side by the fact that the total yearly output must be consumed within one season and on the other by the possibility of imports and increased use of substitutes accompanied by a decreasing demand for butter. The difficulty in the years 1908–10 was that owing to over-speculation and an unwarranted trade optimism business men simply ignored the economic principles underlying the price mechanism. When in January, 1911, the reports came out on the total amount of butter in storage houses, dealers were apprehensive. It exceeded the previous year's storage provision by eighteen million pounds, and taking in consideration that even in 1910 storage butter was not disposed of before the end of April[1] a crisis became inevitable. This was precipitated by the actions of speculators and the storage houses. The former, not having a definite retail trade to rely upon in disposing of a certain amount of their holdings were the first to swamp the market. Outsiders to the trade, they cared little for stability and steadying measures which would have been adopted had the butter been in the hands of dealers. The latter would drop the price steadily, increasing consumption and thus avoiding trade demoralization. With the fall of prices cold storages began to demand additional collateral from the dealers. One morning in January every dealer in Boston received a demand note from the Quincy Storage House to put up $2 per tub. The writer was present at a meeting of dealers on the Produce Exchange at which it was unanimously resolved to refuse in a body the demand for additional collateral. The popular opinion was that the storages must stand by the dealers in a panic after having enriched themselves in the fat years. But the wave could not be stemmed any longer. Failure followed failure. The storage houses left with butter on hand began to throw their holdings upon the overloaded market. Dealers releasing butter at the rate of $16 per tub were glad to sell it at $12. It became evident that it would be impossible to dispose of the supply before new butter should commence coming in. Thus all the profits made within the preceding five years were wiped out only because dealers ceased consulting economics and were carried off their ground by the possibility of sudden fortunes. The high-cost-of-

living problem was, temporarily at least, settled without outside measures—the logic of events which carried the butter price to abnormal heights soon threw it down much below a reasonable minimum.

At present the butter market is seeking its equilibrium and is as a result very convulsive, going up or down with unusual price fluctuation. The explanation lies in the fact that dealers buy only in small quantities and the demand is very sporadic. The price level responds accordingly. Occasional upward movements should therefore not be taken too seriously. On the whole the market shows steadying tendencies and seems to point to the 30-cents-a-pound price which, economically speaking, is the normal price for butter.

M. Lippitt Larkin

Leland Stanford Junior University